DIVIDENDS: THE FOUNDATION OF THE SMART BETA MOVEMENT

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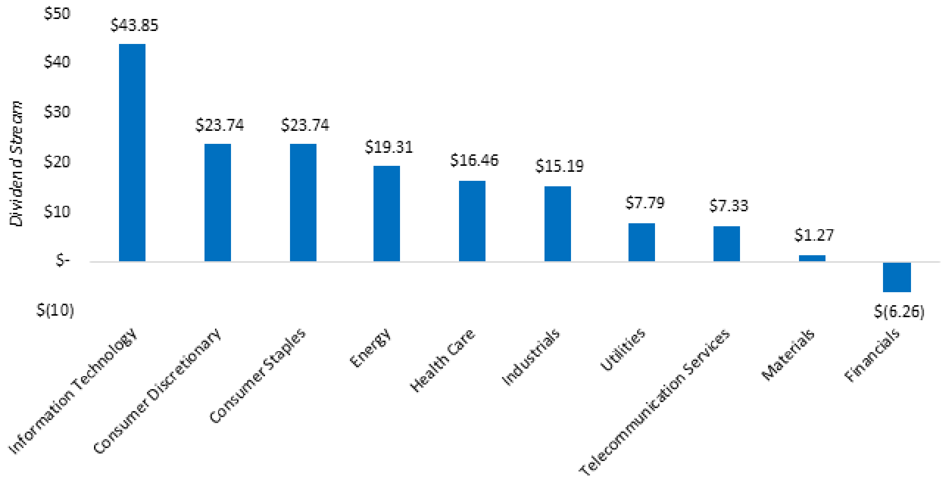
Smart beta exchange-traded funds (ETFs) are rapidly proliferating and capturing assets at a faster clip than the broader ETF industry. In 2015, 143 smart beta ETFs came to market,[1] representing half of the year's new ETF launches, or double the percentage of traditional beta products born last year. Dividend strategies are one of the primary drivers of smart beta ETF growth. Smart beta ETFs had about $616 billion in assets under management at the end of 2015,[2] and more than a quarter of that total was allocated to dividend-oriented funds. Since the publication of the widely followed Fama-French research in 1993, outperformance of fundamentally weighted indexes has mostly been attributed to the market factor, the size factor (mid- and small caps outperforming larger stocks) and the value factor.[3] Later, momentum factor was added as an accepted driver of fundamental weighting's ability to top market cap-weighted strategies. At WisdomTree, we believe weighting by dividends elevates fundamental indexing or smart beta. In 2006, 25 dividend ETFs[4] came to market, 22 of which courtesy of WisdomTree. Our *Dividend Stream®* weighting methodology offers distinct advantages over weighting by market capitalization, dividend yield or focusing on the number of consecutive years that companies have increased payouts. **WidsomTree's Approach to Dividends** WisdomTree dividend benchmarks, such as the WisdomTree LargeCap Dividend Index (WTLDI) and the WisdomTree Dividend Index (WTDI), weight included stocks by utilizing the annual dividend distributions firms have declared they will pay in the coming annual cycle. This forward-looking methodology can help bolster a portfolio's trailing 12-month dividend yield, while factoring in the most up-to-date dividend policies of included constituents. **WisdomTree's Advantage: Flexibility to Reflect Dividend Growth Trends** One of the most exciting illustrations of this principle has been in the Information Technology sector. At our 2007 annual screening, this sector made up only about $16 billion of a $288 billion *Dividend Stream*. But by 2015, it comprised over $60 billion of a $440 *billion Dividend Stream*—an almost fourfold increase.[5] • The WisdomTree Dividend Index saw the Information Technology sector go from a 5% weight after the 2007 rebalance to over a 13% weight after the 2015 rebalance. • The WisdomTree LargeCap Dividend Index saw this sector go from a 6% weight after the 2007 rebalance to almost a 15% weight after the 2015 rebalance. It is also interesting that Financials—approximately one-third of 2007's *Dividend Stream*—are the only sector that hasn't quite returned to its 2007 levels. After the sector's dividend reductions (in some cases government mandated), WisdomTree Indexes took down their exposures. The 2015 *Dividend Stream*—due to the widespread growth across other sectors—is now much better balanced across sectors than was the case in 2007, in our view. **United States *Dividend Stream* Growth by Sector since November 30, 2007 (Pre-crisis) Screening**



Sources: WisdomTree, Bloomberg, with data compared from the 11/30/2007 and 11/30/2015 Index screening dates. Index universe defined as the WisdomTree Dividend Index. You cannot invest directly in an index.

Smart Beta Strategies That Access Multiple Drivers of Returns Another consequence of our focus on dividends is exposure to multiple distinct return premiums—such as value, quality and low volatility. These types of factor tools have been popular of late, now that implementation tools readily exist. However, who would have anticipated that: • 2015 was the year of growth and momentum—so much so that Facebook, Amazon, Netflix and Google, the so-called FANG[6] stocks, came into prominence. • With a simple flip of the calendar, value and lower volatility came back into favor at the start of 2016. **The high-level benefits of our approach to dividends include:** • Broadly inclusive nature that has exhibited a high correlation to established index benchmarks—especially value index benchmarks. • Exposure to more precise size-cuts. These strategies do not introduce small-cap or mid-cap bias through their selection and weighting mechanisms. • Sensitivity to the quality premium. Especially in the United States, there is a signaling aspect to firms declaring a regular dividend, insofar as the belief exists that it can be maintained over time. • Exposure to the low-volatility premium. Going back nearly 10 years, it is not uncommon that our broad-based dividend strategies tend to have betas of .85 to .95 when measured against their market capitalization-weighted benchmarks. While individual factors may come in and out of favor, strategies that combine exposure to multiple drivers of return may be more consistent over time.

[1]Source: Aniket Ullal "A Review of ETF Launches in 2015," Nasdaq, 1/11/16. [2]Source: Attracta Mooney "Smart Beta 'Could Go Horribly Wrong'", Financial Times, 2/22/2016. [3]Source: Robert Dubil, "How Dumb Is Smart Beta? Analyzing the Growth of Fundamental Indexing," Journal of Financial Planning, 28 (3): 49–54. [4]Source: Ben Johnson, "Not All Dividend ETFs Are Created Equal," Morningstar, 4/1/15. [5]Sources: WisdomTree, Bloomberg, with data as of 11/30/15 Index screening. [6]Chris Ciaccia, "What Are FANG Stocks and Why Does Jim Cramer Love Them?," TheStreet.com, 7/24/15.

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DEFINITIONS

Smart Beta : A term for rules-based investment strategies that don't use conventional market-cap weightings.

Dividend : A portion of corporate profits paid out to shareholders.

Fundamental weighting : A type of equity index in which components are chosen based on fundamental criteria as opposed to market capitalization. Fundamentally weighted indexes may be based on fundamental metrics such as revenue, dividend rates, earnings or book value.

Market Factor : Measures sensitivity of a security to the overall market movements.

Size Factor : the average returns of small portfolios minus the average returns of the large portfolios after adjusting for growth or value tendencies.

Value Factor : Characterized by lower price levels relative to fundamentals, such as earnings or dividends. Prices are lower because investors are less certain of the performance of these fundamentals in the future. This term is also related to the Value Factor, which associates these stock characteristics with excess returns vs the market over time.

Momentum Factor : Characterized by assets with recent price increase trends over time. This term is also associated with the Momentum Factor which associates these stock characteristics with excess return vs the market over time.

Market capitalization-weighting : Market cap = share prices x number of shares outstanding. Firms with the highest values receive the highest weights in approaches designed to weight firms by market cap.

Dividend Stream : Refers to the regular dividends per share multiplied by the number of shares outstanding.

Dividend yield : A financial ratio that shows how much a company pays out in dividends each year relative to its share price.

Trailing 12-month dividend yield : Dividends over the prior 12-months are added together and divided by the current share price. Higher values indicate more dividends are being generated per unit of share price.

Annual screening date : The screening date refers to the date upon which characteristics of eligible constituent firms are measured, whereas the rebalance refers to when the results from the screening date are implemented by way of Index weights and constituents.

Rebalance : An index is created by applying a certain set of selection and weighting rules at a certain frequency. WisdomTree rebalances, or re-applies its rules based selection and weighting process on an annual basis.

Value : Characterized by lower price levels relative to fundamentals, such as earnings or dividends. Prices are lower because investors are less certain of the performance of these fundamentals in the future. This term is also related to the Value Factor, which associates these stock characteristics with excess returns vs the market over tim.

Quality : Characterized by higher efficiency and profitability. Typical measures include earnings, return on equity, return on assets, operating profitability as well as others.

This term is also related to the Quality Factor, which associates these stock characteristics with excess returns vs the market over tim.

Volatility : A measure of the dispersion of actual returns around a particular average level. .

Correlation : Statistical measure of how two sets of returns move in relation to each other. Correlation coefficients range from -1 to 1. A correlation of 1 means the two subjects of analysis move in lockstep with each other. A correlation of -1 means the two subjects of analysis have moved in exactly the opposite direction.